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IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 725

In re JAMES CONWAY, trading as Conway Negligees, Conway Beach Togs, and Weehawken Knitting Mills,
Petitioner,

GERALD D. STONE, Trustee, and COMMERCIAL FACTORS CORPORATION,
Appellants.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

JAMES CONWAY, in person.

THE COURT PRESS, N. Y. C.

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GERALD D. STONE, Trustee, and COMMERCIAL FACTORS CORPORATION,
Appellants.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

The undersigned, on behalf of the above named petitioner, pray that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Third Circuit entered on July 1st, 1941 reversing the decision of the District Court of the United States for the District of New Jersey.

Opinions Below.

The opinions of the Court below have not as yet been officially reported. They will be found at pages 25 and 33 of the record.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on June 30, 1941 (R. 33, 34). Jurisdiction

of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925 (28 U. S. C. A. Sec. 347).

Questions Presented.

1. Whether or not the Referee in Bankruptcy erred in adjudicating the debtor a bankrupt when the debtor was solvent and had not committed an act of bankruptcy.

2. Whether or not the Referee in Bankruptcy erred in adjudicating the debtor a bankrupt in accordance with Section 376 (2) of the Chandler Act without an examination of the debtor, which is mandatory, as required by Section 336 (3) of the Chandler Act.

Statutes Involved.

The statutes involved are Sections 376 and 336 (3) of the Chandler Act.

Statement.

James Conway filed a petition for an arrangement under Section 322 of Chapter XI of the Chandler Act. That thereafter notices were duly sent out by the Referee in Bankruptcy advising creditors of the said James Conway that a first meeting of creditors would be held pursuant to Section 336 of said Act. Thereafter, said meeting was held and subsequently upon a vote duly taken, the said James Conway was unable to secure a majority of consents to his Plan of Arrangement from his creditors. Thereafter, notices were sent out by the said Referee in Bankruptcy ad-

vising that in accordance with Section 376 of the Chandler Act, the Referee in Bankruptcy would decide whether or not to adjudicate or dismiss the proceedings in accordance with the said Act. Said meeting was held on October 25th, 1940 and the said James Conway was adjudicated a bankrupt. On the 4th day of November, 1940, the said James Conway filed a petition for review with the Referee in Bankruptcy contesting the said order of adjudication. The matter duly came on before Judge Guy L. Fake of the United States District Court and by order dated December 11th, 1940 the said adjudication was set aside and the matter was referred back to the Referee to hold a proper meeting in accordance with Section 336 of the Chandler Act.

Thereafter a new first meeting of creditors was held by the Referee in Bankruptcy in accordance with Section 336 (3) of the Chandler Act and the debtor, for the first time, was duly examined. The Referee thereafter set the 11th day of February, 1941 as the last day of filing consents to the Plan of Arrangement.

Section 376 (2) of the Chandler Act provides in substance that where a Plan of Arrangement is not accepted by creditors after due notice to creditors, the Court may adjudicate or dismiss whichever in the opinion of the Court is for the best interest of the creditors.

On the 11th day of February, 1941, the Referee in Bankruptcy, again adjudicated the debtor a bankrupt, holding that the debtor did not have sufficient consents to his plan of arrangement. The Referee permitted three creditors to withdraw their consents from the plan of arrangement. The debtor submitted a new petition for review of the Referee's decision, and same was duly granted by the District Court,

which Court held consents to the arrangement could not be withdrawn in the absence of fraud or misrepresentation. The District Court returned the matter to the Referee in Bankruptcy and directed him to proceed with the arrangement. In the interim an appeal was taken to the Circuit Court of Appeals, Third Circuit, from the order of the District Court dated December 10, 1941 and on June 30, 1941 the said Circuit Court of Appeals (R. 33) unanimously reversed Judge Fake and reinstated the adjudication of October 25th, 1941, and by its mandate (R. 33) directed that liquidation be proceeded with.

In the case at bar, the record is void of any facts or information which guided the Referee in adjudicating the debtor herein a bankrupt. The only record before the Referee was the petition filed by the debtor herein. The petition filed by the debtor showed the following conditions to exist:

The debtor owed approximately $44,500.00 to unsecured creditors and to preferred creditors, including taxes, approximately $9,000.00. The debtor's assets consisted of the following:

Approximately $21,000.00 of Accounts Receivable, around $5,000.00 in banks, saleable inventory of approximately $32,000.00, merchandise and machinery of approximately $18,000.00 and other assets amounting to $1,000.00. The debtor clearly had an excess of assets over liabilities of $23,000.00. The petition further showed that the debtor was engaged in the negligee business. It is common knowledge that the negligee business is primarily a Christmas business so that at the time of the adjudication, which was October 25th, 1940, the debtor was in a more liquid posi-

tion than he was at the time of the filing for a petition of arrangement.

From the record before the Referee at the time of his deciding whether to adjudicate or dismiss, it becomes self-evident that the best interest of creditors would be served by dismissing the arrangement proceedings, than to adjudicate the debtor a bankrupt. It is common knowledge that assets sold at liquidation bring a fraction on the dollar of their actual value. Furthermore, the $21,000.00 of Accounts Receivable existing at the time of the filing of the petition were practically collected, as it is a known fact that in the negligee business the terms of sale average 5/10 Eom.

Specification of Errors.

The Circuit Court of Appeals erred:

(1) In reversing the order of the District Court.

(2) In holding that it was not necessary to find that the debtor was insolvent before he could be adjudicated a bankrupt under Section 376 (2) of the Chandler Act.

(3) In so construing Section 336 (3) of the Chandler Act as to hold that the examination of the debtor under said section could be waived by the debtor, and that said section was no right of the debtor, but solely a right for creditors and the Referee.

(4) In holding that its said construction and application of said statutes did not violate the Fifth Amendment to the Constitution.

Reasons for Granting the Writ.

In holding that petitioners need not be examined under Section 336 (3) of the Chandler Act, and that insolvency is not a prerequisite under Section 376 (2) of the Chandler Act, the Circuit Court of Appeals decided important questions of federal law which have not been, but should be, settled by this Court (Rule 38 (5) (b)).

(1) No Court other than the Court below has interpreted Sections 336 (3) and 376 (2) of the Chandler Act so as to take away one's property without a proper hearing and without a finding of insolvency.

Section 336 of the Chandler Act, Subdivision (3) provides as follows:

> "At such meeting or at any adjournment thereof, the Judge or Referee shall examine the debtor or cause him to be examined and hear witnesses on any matter relative to the proceeding."

This section was derived from the old act, Sections 12A and 74D. Under the law statutes this examination by the Referee was a permissive statute. With the enactment of the Chandler Act this section was changed so as to make it mandatory upon the Referee in Bankruptcy to hold an examination of a debtor. The reasons for the change become self-evident after slight thought. The Chandler Act was enacted to afford individuals or corporations who were unable to pay their debts as they mature, an extension of time for the payment of same. Congress in enacting the Chandler Act found fault with the old bankruptcy laws and decided that the best interests of all

parties concerned would be served by having debtors examined by the Referee. With such an examination, the creditors would be in a position to determine whether or not to accept a proposed Plan of Arrangement. It is a known fact that while a debtor will list in his schedules numerous assets, it is necessary for someone to inquire into the nature of the business of the debtor and ascertain whether or not the proposed Plan of Arrangement is feasible and fair under the circumstance. Without an examination as required by Section 336 of the Chandler Act, Subdivision (3), it is conceivable why creditors in the case at bar refused to accept the proposed Plan of Arrangement calling for payment of One Hundred (100%) Per Cent over a period of time. Since the reversal by Judge Fake, the Referee held an examination of the debtor pursuant to the said Section 336, the debtor has been able to secure a majority of consents in number and amount as required by the Act. It therefore becomes apparent that the argument of the Circuit Court that the failure to examine is a harmless error, is absurd on its face. If the error was harmless and the examination intended by the Act was to be a cursory one, why is it that since the examination was held that the debtor was able to obtain sufficient consents to his Plan of Arrangement; *after having been examined at the meeting of creditors.*

> See Congressional Record, June, 1937 re Chandler Act.

An examination under Section 336 serves another purpose than that of advising creditors as to the possibility of accepting a Plan of Arrangement. In the event a Plan of Arrangement is not accepted, the secondary purpose of the examination is to afford a

Referee in Bankruptcy, when he comes to Section 376 of the Act, an opportunity to decide upon facts what is the best interest of creditors, in regard to whether to adjudicate or dismiss the proceedings. By examining the debtor at the first meeting of creditors, the Referee in Bankruptcy is able to ascertain whether or not the best interest of creditors will be served by adjudicating the debtor concern a bankrupt or in dismissing proceedings. In the case at bar, we find that no such examination as required by the Act was held. It is hard to understand upon what grounds the Referee decided what the best interest of creditors would be served by adjudicating the debtor a bankrupt herein. The only thing before him was the petition filed by the debtor. If that was the source of his information then the Referee erred in adjudicating the debtor a bankrupt herein. The reason is that the petition showed $23,000.00 of assets over liabilities.

The Circuit Court, in holding that the examination of the debtor under Section 336 (3) in no wise affects a debtor, but is merely for the guidance of creditors, the Referee assumed that the debtor has no rights to the examination, all of which is fallacious. The purpose of the new Chandler Act was to permit honest individuals, engaged in business, to continue in business, by obtaining for them an extension of time to pay their obligations. In the case at bar, the debtor had been in business for over eighteen years, untainted by fraud or chicanery, desirous of paying his creditors over a period of time. Can it be said that the debtor had no interests or rights in the proceedings, or that the failure to examine was harmless error? The Circuit Court goes to great length in its opinion (R. 29) to stress the purpose of the Bank-

ruptcy Act, quoting Senator Ingalls of Louisiana to the effect that "* * * to destroy an honest business house where he has an abundance of assets to meet every obligation would seem an act of wantonness which ought not to be tolerated * * *" yet in the next breath it destroys the business of the debtor, claiming that he should not bite the hand that dispenses mercy to him. In elementary dialectics the logic of the Circuit Court would be a *non sequitor*. The ruling of the Circuit below is most novel and strange, it would work undue hardships and misfortune upon debtors to the extent that the powers of this Court should be invoked to clarify the situation and interpret the Chandler Act so that it will carry out the intention of Congress to alleviate the misery of honest business people who find themselves in a solvent but frozen condition. To permit debtors to be adjudicated without the necessary examinations as to their assets and liabilities, and as to the best manner of conducting the proceedings, would beyond a peradventure of a doubt, violate the fifth amendment (*Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, 589 (1935); *Monongahela Navigation Co.* v. *United States*, 148 U. S. 312, 336 (1893); *Kuehner* v. *Irving Trust Co.*, 299 U. S. 445, 451 (1937)).

The present business conditions warrant liberal bankruptcy laws, not for the dishonest and mountebank, but for the man of integrity, who, through conditions beyond his control, finds himself unable to pay his debts as they mature. What a travesty and mockery it would be to destroy a business whose only crime is that the sweeping tide of world unrest has caused them to enter our bankruptcy courts seeking relief, only to be told you have no rights, don't complain, else you are an "ungrateful scoundrel". The

Circuit Court in its opinion seems to lay great stress on the purpose of the Bankruptcy Act, then with the speed of a bolt of lightning, makes a complete somersault and says don't bite the hand that feeds you (R. 31). To follow the logic of the Circuit Court, the conclusion is inevitable that a debtor has no rights, to attempt to protest such an arbitrary and capricious ruling brands him as an ingrate.

This Court cannot in good conscience permit this honest debtor, James Conway, or others, who may be so unfortunate in the future, to be deprived of their life's work and toil without a hearing or examination which is mandatory by Section 336 (3). To permit such a condition to exist would circumvent the purpose of the Chandler Act and make honest men shun the supposedly welcome arms of the bankruptcy courts when they are in distress. Public policy demands that a debtor be examined before he can be adjudicated, especially where he is solvent.

Conclusion.

In adjudication the petitioner a bankrupt without the mandatory examination required by Section 336 (3) the Court below acted capriciously and violated the Fifth Amendment which act should be reviewed by this Court.

WHEREFORE, it is respectfully submitted that this petition for a writ of certiorari should be granted.

JAMES CONWAY,
Debtor in Person.

State of New York,
City of New York,
County of New York—ss.:

GEORGE HOROWITZ, being duly sworn, deposes and says that he is the counsel for James Conway, petitioner herein; that he has read the foregoing petition and knows the contents thereof, and that the same is true to his own knowledge, except as to the matters therein stated to be alleged upon information and belief, and as to those matters he believes it to be true.

That the within record and writ of certiorari have been filed one month late, for the reason that your deponent erred in computing his time to prepare the said papers. This matter is of vital concern to the client and would prove very detrimental to him, to punish him for the error of counsel. This request is being most humbly made by the errant.

Deponent further says that the reason this verification is made by deponent and not by James Conway is because the said petitioner is a New Jersey resident, and deponent is its counsel.

GEORGE HOROWITZ.

Sworn to before me this
30 day of October, 1941.

ROBERT B. NATHAN,
Notary Public,
New York County.